

**IN THE
SUPREME COURT OF MISSOURI**

No. 83870

**EDDIE BAUER, INC.,
Appellant,**

v.

**DIRECTOR OF REVENUE,
Respondent.**

**On Petition for Review from the
Missouri Administrative Hearing Commission
Honorable Sharon Busch, Commissioner**

**REPLY BRIEF OF AMICUS CURIAE
THE KROGER CO. AND SUBSIDIARIES**

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ARGUMENT

Introduction

Eddie Bauer filed Missouri income tax returns and admittedly overpaid its Missouri income tax because it was denied the right to file its returns and pay its tax as part of a consolidated group as the result of the unconstitutional fifty percent restriction in Section 143.431.3(1). *See General Motors Corp. v. Director of Revenue*, 981 S.W.2d 561 (Mo. banc. 1998) (the fifty percent threshold requirement in Section 143.431.3(1) violated the Commerce Clause of the U.S. Constitution). The question now is whether the Attorney General’s creative arguments and contrived procedures can support the Director’s denial of any effective relief to Eddie Bauer from the consequent overcollection of its tax.

The Director argues that Eddie Bauer had constitutionally adequate pre- and post-deprivation remedies that it either failed to invoke or improperly invoked. Specifically, the Director argues that Eddie Bauer should have done as GM did—violate Section 143.431.3(1) and the Director’s regulation thereunder by “timely” filing on a consolidated basis and protest the resulting notice of deficiency and its consequent penalties (Dir. Br. Pt. I). In making this argument, the Director downplays the assessment of penalties inherent when a taxpayer intentionally disregards regulations. She does this by relying on a case construing an entirely different penalty standard under the use tax law. Alternatively, the Director argues that Missouri’s refund statute provides an adequate remedy (Dir. Br. Pt. II). Since that is the remedy Eddie Bauer invoked, the Director argues that Eddie Bauer failed to “properly pursue” it because there was no “timely” election to file on a consolidated basis and because Eddie Bauer did not seek the refund of tax it overpaid. In the Director’s opinion, Eddie Bauer could have properly invoked this remedy by “timely” filing on a separate company basis *and* by “timely” filing as part of a

consolidated group, paid tax twice (once under each filing), sought the refund of tax paid under each basis, and appealed the refund denial(s). In short, Eddie Bauer had the Director's "remedy" if it met the condition that it loan the Director money above and beyond what even the Director claims is due. This argument is one that the Director never made below and was not considered by the Commission.

The Director also argues that Missouri did not withdraw any post-deprivation remedy (Dir. Br. Pt. III), that suits for injunction and declaratory relief were adequate remedies (Dir. Br. Pt. IV), and that Eddie Bauer's refund claim for 1995 was, in any event, untimely (Dir. Br. Pt. V). The latter argument is not addressed herein because it is not applicable to *Amicus* Kroger.

The Director's arguments are all premised upon misapplications of law. **First**, as the Director concedes, any remedy that subjects a taxpayer to a risk of penalties is a constitutionally inadequate remedy. Because the pre-deprivation procedure the Director proposed would have subjected Eddie Bauer to penalties, it was inadequate as a matter of law. **Second**, Eddie Bauer's and Spiegel's election to file on a consolidated basis was a valid election in that the Director's regulatory deadline was a practical impossibility because of the illegal fifty percent threshold. *See* Eddie Bauer's and Kroger's opening briefs. **Third**, a refund is required under the refund statute because, having made an election to file on a consolidated basis, the parent is entitled, and in fact is required by the Director's regulation 12 CSR 10-2.045(32), to file a refund claim for any tax overpaid by it and its members for any year a consolidated income tax return has been filed. **Fourth**, injunctive and declaratory relief are inadequate remedies because, even if taxpayers had inadequate remedies at law, those equitable remedies operate prospectively only.

I. There Is No Adequate Pre-Deprivation Remedy

The Director argues that Eddie Bauer had an adequate pre-deprivation remedy and should have done what GM did--violate Section 143.431.3(1) and the Director's regulation thereunder by "timely" filing on a consolidated basis and protest the resulting notice of deficiency and its consequent penalties (Dir. Br. Pt. I). The obvious problem with this "remedy" is that Eddie Bauer, like GM, would have been subject to the assessment of substantial penalties (GM was assessed almost \$700,000 in penalties) and, as the Director practically concedes, the risk of penalties makes a remedy constitutionally inadequate. *McKesson Corporation v. Division of Alcoholic Beverages and Tobacco*, 496 U.S. 18, 38 (1990). To avoid this conclusion, the Director argues that a use tax penalty standard would have prevented the assessment of income tax penalties against Eddie Bauer, an argument that is disingenuous at best.

Section 143.751.1 provides that any "deficiency ... due to ... intentional disregard of rules and regulations ... shall" result in the imposition of a five percent addition to tax. GM violated the Director's regulation because GM did not meet the fifty percent threshold. The Director would have this Court ignore the plain meaning of Section 143.751.1 by relying on *Hewitt Well Drilling & Pump Service, Inc. v. Director of Revenue*, 847 S.W.2d 795, 799 (Mo. banc. 1993). There, this Court construed Section 144.655.1, which imposed use tax additions "unless it is shown that such failure [to file a use tax return] is due to reasonable cause and not the result of willful neglect, evasion, or fraudulent intent." This Court resolved the "seemingly irreconcilable conflict" in that standard, by requiring taxpayers to show an absence of willful neglect. The Director suggests that, in view of the U.S. Supreme Court's opinion in *Kraft General Foods, Inc. v. Iowa Dep't of Revenue*, 505 U.S. 71 (1992), Eddie Bauer could show a lack of willful neglect.

But the *Hewitt* decision did not purport to construe the language of Section 143.751.1, or language remotely similar thereto, and is completely inapposite. There is no possible claim that Eddie Bauer failed to file a return, the event at issue under Section 144.655.1, nor does this case involve use tax. This Court's decision in *Hewitt* certainly does not put anyone on notice that Section 143.751.1 would not apply to Eddie Bauer. The Director attempts to reconcile her argument with the fact that she did assess almost \$700,000 in additions against GM. She argues that *Hewitt* was decided before the tax periods at issue in GM, but prior to the tax periods at issue here. That fact is irrelevant since the Director assessed the \$700,000 penalty against GM on July 26, 1996, well after *Hewitt* was decided. *See General Motors Corporation and Subsidiaries v. Director of Revenue*, No. 96-1882RI (Mo. Admin. Hrg. Comm'n, May 4, 1998), Finding of Fact 24.

In summary, there was no constitutionally adequate pre-deprivation remedy because the only such "remedy" the Director identified posed a serious risk of penalties.

II. Eddie Bauer Properly Invoked the Refund Remedy

The Director argues that the post-deprivation refund claim procedure in Section 143.801.1 is a constitutionally adequate safeguard against the illegal collection of taxes, but that Eddie Bauer and its affiliates are not entitled to relief under this procedure because they "did not properly use it" (Dir. Br. 18-19). In support of this proposition, the Director notes that the refund claims in dispute were filed not by the taxpayer Eddie Bauer itself, but rather by Eddie Bauer's parent company, Spiegel, Inc. under the business name "Spiegel, Inc., Eddie Bauer, Inc., and Combined Affiliates." *Id.* The Director also argues that Spiegel cannot act on behalf of Eddie Bauer because Spiegel never timely elected to file on a consolidated basis.

Eddie Bauer and *Amicus* Kroger addressed in detail in their opening briefs the Director’s claim that Eddie Bauer’s consolidated return filings were nullities because it allegedly did not meet the Director’s election deadline. As explained, if it failed to meet that deadline, it was only due to the operation of the illegal fifty percent threshold. The State is free to raise procedural requirements governing refund claim actions, even when the requirements may operate to deny a taxpayer relief from illegal taxes. *McKesson Corp.*, 496 U.S. at 45; *James M. Beam Distilling Co. v. Georgia*, 501 U.S. 529, 544. However, a State may not invoke those procedural requirements to deny a taxpayer relief from the State’s collection of unconstitutional taxes where, as here, the procedures themselves are invalid. As the Director stipulated, when Eddie Bauer filed its original returns for the years at issue, Eddie Bauer and its affiliates *were prohibited* from making the consolidated return election by the fifty percent threshold requirement this Court later struck down in *General Motors Corp.* (L.F. 44). Therefore, if the declaration of the invalidity of the fifty percent threshold is to have meaning, no effect can be given to the Director’s election deadline.

The Director’s other claim, that Spiegel could not seek a refund of tax its affiliate overpaid, is directly contrary to the Director’s regulation 12 CSR 10-2.045(32) and to the spirit and intent of the consolidated return filing procedure. Regulation 12 CSR 10-2.045(32) provides that “[t]he **common parent will file claims for refund or credit, and any refund will be made directly to and in the name of the common parent and will discharge any liability of the state of Missouri in respect thereof to any subsidiary member[.]**” [emphasis added].

Furthermore, 12 CSR 10-2.045(40), under some circumstances, imposes upon the separate companies of a consolidated group filing a consolidated return, the obligation to, nevertheless, make estimated Missouri income tax payments on a separate company basis. Those payments are then

credited against the liability of the consolidated group. If the consolidated group's tax liability is less than that already remitted by its affiliates, a refund can be issued only to the parent under 12 CSR 10-2.045(32).

The above regulation makes it abundantly clear that Eddie Bauer's filings in this matter were in complete compliance with the Director's regulation. Furthermore, it is clear from the application of Section 143.431.3(1) that the consolidated group and its members are, for purposes of Missouri's income tax law, the "taxpayer." Any common sense reading of Section 143.801 would consider as the "taxpayer" the entity that is responsible for paying the tax on behalf of the consolidated group and its members. Here, that entity is Spiegel. The Director's hypertechnical arguments to the contrary are misplaced.

The Attorney General and Director recognize that Missouri must afford taxpayers like Eddie Bauer some form of relief from the illegal collection of tax as a result of the fifty percent threshold. Thus, the Attorney General suggests a way to invoke the post-deprivation refund remedy, but still avoid all of the creative roadblocks the Director has allegedly erected. Specifically, the Attorney General claims that in order to avoid what he euphemistically calls the "problematic" language in the Section 143.431.3(1), the language this Court severed from the statute in *General Motors Corp.*, Eddie Bauer should have elected what the Attorney General describes as the "dual-filing" option (Dir. Br. 20-21). According to the Attorney General, under this "dual-filing" option, Eddie Bauer should have filed income tax returns and paid its income taxes *twice*: once in its own name, on a separate company basis; and again in Spiegel's name, on a consolidated basis. *Id.* That way, the Attorney General reasons, Spiegel could have made itself the "taxpayer," and would therefore have been eligible for a refund if the "problematic" language in Section 143.431.3(1) was ever stricken. *Id.*

This “dual-filing” alternative is no alternative at all. Whatever procedural safeguards a state may adopt, that is, pre-deprivation, post-deprivation, or some combination of the two, due process requires a “clear and certain” remedy for taxes collected in violation of the Constitution. *Reich v. Collins*, 513 U.S. 106, 111; *McKesson Corp.*, 496 U.S. at 39; *Atchison, T. & S.F.R Co. v. O’Connor*, 223 U.S. 280, 285 (1912). The remedial alternative proposed by the Attorney General falls far below this standard. A remedy is “clear and certain” in the constitutional sense when the average taxpayer would conclude that the remedy is actually available. *Reich*, 513 U.S. at 111. The average taxpayer reviewing Missouri’s revenue laws would not conclude that the “dual-filing” alternative is available, as either a pre- or post-deprivation remedy, because the so-called option is nowhere contemplated, much less actually authorized, by those laws.

Furthermore, and even more damaging to the Attorney General’s argument, is the fact that this newly proposed remedy exacts a penalty for its exercise. In order to avail itself of that “remedy,” a taxpayer must not only pay the Director the amount she claims is due, but must also invest additional funds as a prerequisite to challenging an unconstitutional deprivation of its property. Because the Director would pay interest on whatever amount is eventually returned to the taxpayer, the precondition of this remedy can be described as nothing short of a compulsory loan. The taxpayer must pay tax twice, and in the case where a consolidated filing provides only marginal tax savings, the amount the taxpayer must pay approaches twice the amount the Director claims is due. The requirement that a taxpayer loan the Director money is merely another form of penalty. Therefore, under *McKesson*, the Director’s newly articulated “remedy” is constitutionally impotent as well.

Therefore, Spiegel and Eddie Bauer were entitled to file a consolidated return for the tax periods, and Spiegel was entitled to seek a refund of tax collectively overpaid by members of the consolidated group.

III. The Director has Engaged in Bait and Switch Tactics

In *Reich v. Collins*, 513 U.S. 106 (1994), the Supreme Court held that a state may not hold out a “clear and certain” post-deprivation remedial procedure and then deny a taxpayer relief on the ground that the taxpayer could have chosen a pre-deprivation alternative. *Id.* at 113; *see Newsweek, Inc. v. Florida Dep’t of Revenue*, 522 U.S. 442, 444 (1998). The Director argues that there has been no remedial “bait-and-switch” here because Eddie Bauer and its affiliates were barred from pursuing the post-deprivation refund claim alternative in Section 143.801.1 in the first place (Dir. Br. 21-23). This argument is based on the same, constitutionally false premise that Eddie Bauer and its affiliates “did not properly use” the State’s refund claim procedures.

Once again, if Eddie Bauer and its affiliates (*i.e.*, the Spiegel Group) did not timely make the consolidated return election, if Spiegel, Inc. itself was not a “taxpayer” and thus was not eligible to file refund claims under Section 143.801.1, it was only because of the law that this Court later declared unconstitutional in *General Motors Corp.* The argument that there has been no “bait-and-switch” because Eddie Bauer and its affiliates were legally foreclosed from pursuing post-deprivation relief, therefore, cannot be sustained. Furthermore, the Director’s claim in this regard is refuted by her regulation 12 CSR 10-2.045(32), which provides that only the parent may seek a refund of overpaid tax, and expressly forbids the subsidiary from making such a claim in any year where there has been a consolidated filing. Only after Eddie Bauer followed the procedure 12 CSR 10-2.045(32) set, did the

Director argue that such a procedure was inadequate. No clearer bait and switch tactics can be envisioned.

IV. Injunctive and Declaratory Relief are Irrelevant

The Director claims that in addition to the remedies provided by the income tax laws, there is yet another, equitable remedial procedure Eddie Bauer and its affiliates might have pursued. Specifically, the Director speculates that Eddie Bauer might have been able to challenge the validity of the fifty percent threshold by seeking declaratory and injunctive relief (Dir. Br. at 23-24). This argument is without merit.

In *McKesson Corp.*, 496 U.S. 18 (1990), the Supreme Court found that after holding a state liquor tax unconstitutional, the Florida Supreme Court correctly awarded the petitioner declaratory and injunctive relief against continued enforcement of the offending statute. *Id.* at 31. In so doing, however, the Court held that by itself, this form of prospective relief did not satisfy Florida's obligations under the Due Process Clause. *Id.* Specifically, the Court held that if a state "places a taxpayer under duress promptly to pay a tax when due and relegates him to a postpayment refund action in which he can challenge the tax's legality, the Due Process Clause of the Fourteenth Amendment obligates the state to provide meaningful backward-looking relief to rectify any constitutional deprivation." *Id.*

The Director suggests that Eddie Bauer could have challenged the fifty percent threshold requirement through an action in equity. Yet, the Director argues at the same time that Eddie Bauer and its affiliates are not entitled to retrospective relief because Eddie Bauer "did not properly use" the remedial procedures provided by law. The rule in *McKesson Corp.* prevents the Director from placing Eddie Bauer in this constitutional box. Therefore, declaratory and injunctive relief are constitutionally inadequate in and of themselves; Eddie Bauer must be afforded a remedy to recover its

payment of illegal taxes. That remedy, and the one Eddie Bauer invoked, is the statutory claim for refund.

CONCLUSION

The Commission erred in determining that Eddie Bauer and its affiliates were barred from invoking the post-deprivation refund claim procedures in Section 143.801.1 and that Eddie Bauer was thus relegated to the constitutionally inadequate pre-deprivation protest alternative in Section 143.631. The contrary arguments in the Director's brief notwithstanding, the Commission's interpretation of these remedial procedures cannot be squared with the constitutional doctrine of remedies articulated by the U.S. Supreme Court's recent state tax cases. Based on the foregoing, *Amicus* Kroger respectfully suggests that the decision below should be reversed, and that Eddie Bauer's refund claims should be granted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that two true and accurate copies of the foregoing were mailed first class, postage prepaid, this ____ day of December, 2001, to State Solicitor James Layton, P.O. Box 899, Jefferson City, Missouri 65102, Attorney for the Director, to Marilyn A. Wethekam, Fred O. Marcus and Brian L. Browdy, 180 N. LaSalle Street, Suite 3700, Chicago, Illinois 60601, and to Janette Lohman, Michael Annis, and Eric G. Enlow, 720 Olive Street, 24th Floor, St. Louis, Missouri 63101, Attorneys for Appellant.

CERTIFICATE REQUIRED BY SPECIAL RULE 1(C)

I hereby certify that the foregoing brief includes the information required by Supreme Court Rule 55.03 and complies with the limitations contained in Supreme Court Special Rule 1(b). The foregoing brief contains 3,418 words.

The undersigned further certifies that the disk simultaneously filed with the briefs filed with this Court under Supreme Court Rule 84.05(a) has been scanned for viruses and is virus-free.
